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C O N F I D E N T I A L SECTION 01 OF 02 LJUBLJANA 000567

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SUBJECT: PETROL DOES DEAL WITH LUKOIL AND HARRAH'S SHOULD
ALLAY LOCAL FEARS TO MOVE AHEAD

REF: LJUBLJANA 386 (AND PREVIOUS)

Classified By: COM Thomas B. Robertson for reasons 1.4 (b) and (d)

1.(C) Summary: COM hosted lunch for Viktor Baraga, Chairman of both the Petrol supervisory board and the HIT (casinos) supervisory board, (and childhood friend of Prime Minister Janez Jansa) on August 23. Baraga, a successful businessman, described to us the Slovenian approach to the economy which we think accurately reflect this government's implied if not openly stated approach to privatization and foreign direct investment. Baraga was candid about Slovenia's desire to preserve and even expand Slovenian companies by keeping them in Slovenian hands, even if that meant the government's hands; the desire for the GOS to develop joint ventures that ensured it retained majority ownership; and the strong belief that Slovenia could successfully continue its privatization process at a much more measured pace than its neighbors to the east.

12. (C) As a businessman, Baraga agreed that the Government is not the best manager of companies. However, as a Slovenian, he had to acknowledge that in a country as small as his, the various hidden agendas would continue to manipulate and influence any plans for privatization and expansion of Slovenian companies. In his position as chairman of the supervisory board of HIT, Baraga claimed that he was not deeply into the details of the potential deal between HIT and Harrah's' but he did recommend that Harrah's raise its profile both with the Government (Prime Minister, Finance Minister) and within the Nova Gorica community. During lunch Baraga also foreshadowed the transformation of Petrol into a holding company and the plans for a joint venture with Russia's Lukoil - which was subsequently announced on August 28 on the margins of the Bled Strategic Forum. END SUMMARY.

BARAGA: CLOSE CONFIDANT OF PRIME MINISTER

13. (C) Over the last year to eighteen months, Prime Minister Jansa has been accused by his political opponents of stacking supervisory and management boards of nearly all partially government owned Slovenian companies with hand-picked cronies, sometimes of questionable competence. This is, in practice, no different than actions of predecessor governments, and on the whole, the GOS has picked competent people to assume stewardship of Slovenia's crown jewels. Viktor Baraga is a well established business person in his own right who runs a trading company based in Melbourne, Australia. (He also has the title of Honorary Consul of Australia in Slovenia). In his meeting with COM, Baraga

acknowledged that his position on the boards of HIT and Petrol had something to do with his friendship with Jansa. He also emphasized that he had accepted the jobs somewhat reluctantly, but he gave every indication that he felt fully qualified for the responsibility. It was clear that he and the Prime Minister are in regular contact on issues related to both Petrol and HIT. Baraga was also straightforward about the nature of his position, and given that political winds could easily blow him off both boards, his first responsibility was to ensuring the health and viability of his own business, because that's "where (his) bread is buttered."

14. (C) Viktor Baraga's position on both the Petrol and the HIT boards allows for a reliable insight into the real intentions of the GOS and how it plans to expand and diversify Slovenia's economy. Despite his decades of exposure to western business practices, Baraga accepts the GOS will continue to pursue the "go slow" school of economic reform and privatization in Slovenia. He has a personally more pragmatic view of what is best for the economy and no fear of foreign investors, but events over the last year indicate that while the political will for reform exists, political realities (upcoming local elections) dictate reform be introduced in measured doses. Baraga explained the GOS view in very blunt terms saying that while the Government is not the best manager of business, selling out to a foreigner would be the GOS's choice of "last resort" and if a business is doing well, there is no need to rush the divestiture. On the other hand, the GOS is always interested in attracting "strategic" partners. (Note: this tends to be a minority partner with capital to inject into the venture, sometimes with a promise to increase holdings in the future, but always

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short of majority. End Note) Baraga described plans to turn Petrol into a holding company and to then pursue a joint venture deal, creating a new company, with Russia's Lukoil. This very scenario was revealed to the public five days later on the margins of the Bled Strategic Forum.

PETROL PENS DEAL WITH LUKOIL

5.(U) In this deal, Petrol Lukoil (PL), as the company will be known, will jointly own all the Petrol outlets in Slovenia and plans to double its retail network expanding through out the Western Balkans by 2009; increase revenues to 4.5 billion euros; and report profits of over 75 million euros. The new company will be 51% owned by Petrol and 49% owned by Lukoil. Lukoil's outlets in Romania, Bulgaria and Hungary were not part of the deal because Petrol would not have been able to retain 51% ownership. With this deal, Minister of Economy Andrej Vizjak was apparently also able to pressure Lukoil to at least consider investing in the rehabilitation of Slovenia's sole oil refinery in Lendava, near the Hungarian border. The Slovenian press, describing Petrol CEO Marko Kryzanowski as "thrilled" over the deal, has expressed some skepticism that it will ever get off the ground citing past behavior of Petrol's MOU to produce electric energy with Austrian company Estag which lapsed after nearly three years of inactivity.

HARRAH'S: NEED TO ENGAGE THE PUBLIC AND ASSUAGE FEARS

6.(C) Baraga's message on the HIT/Harrah's deal was clear - the Prime Minister would like a deal to happen, the Finance Minister would like the deal to happen, although he is perhaps less enthusiastic about the project, and Harrah's will need to do some public relations work to alleviate fears that it's casino will cannibalize existing casinos in the region putting many jobs, including those of management and

management board members, at risk.

7.(C) Baraga suggested that Harrah's might consider modifying its approach to the deal and consider it as a strategic investment, thus leaving 51% ownership in the hands of the Slovene partner. He noted Harrah's could still go forward with its investment plan and maintain its control by insisting on the management board having someone Harrah's would select running things for the first 4-5 years, followed by HIT. The bottom line for the GOS, and particularly Finance Minister Bajuk was that whatever the configuration of the deal and the project, its revenue would not drop, nor would the number of people employed.

COMMENT

18. (C) The deal between Petrol and Lukoil does not come as a great surprise, especially given that the GOS/Petrol seems to have managed to secure a 51% share of the new company. It would have been very surprising if the percentages had gone the other way. Also interesting is that both the press and, in private conversations, our official contacts, wants the "American Reaction," expecting us to raise serious concerns about such a deal with Russia. Our response has been that "we support diversity in energy supplies and transparency in commercial deals." The Lukoil deal is also very interesting to look at in light of the other big deal sitting in Slovenia's lap, the Harrah's casino proposal. The agreement to go forward with Lukoil is no doubt a result of Petrol's maintaining a 51% share, and hence control, of the business activities of this new venture. Part of the slowness of the Harrah's/HIT negotiations are a result of Slovenian fears, especially on the local level (HIT), as Baraga has understood them, that if Harrah's has a majority share of HIT, Slovenian control will be lost with possible regrettable consequences. Harrah's will continue negotiations with HIT in September, and we hope we will have a better indication after those meetings of whether Slovenia is prepared to forward with a mega deal and what share of ownership will be required. End Comment.
ROBERTSON